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NO. 211

LONE STAR GAS COMPANY,

Appellant

Versus

THE STATE OF TEXAS, ET AL.

Appellees

APPEAL FROM THE COURT OF CIVIL APPEALS
FOR THE THIRD SUPREME JUDICIAL DISTRICT
OF TEXAS AT AUSTIN

SECOND SUPPLEMENTAL BRIEF FOR
APPELLEES

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, A.D. 1937

NO. 313

LONE STAR GAS COMPANY,
Appellant

Versus

THE STATE OF TEXAS, ET AL,
Appellees

APPEAL FROM THE COURT OF CIVIL APPEALS FOR THE THIRD SUPREME JUDICIAL DISTRICT OF TEXAS, AT AUSTIN

SECOND SUPPLEMENTAL BRIEF FOR APPELLEES

MAY IT PLEASE THE COURT:

Appellant delivered to us, on April 6, 1938, copies of "Appellant's Reply To Appellees' Supplemental Brief." Insofar as we have been advised, the Court has not authorized the filing of such additional brief by appellant, but we have no objection thereto if it will be of any aid to the Court; but if filed, as we presume it has been, it necessitates this additional brief from us in

order to correct some additional misleading and erroneous statements and contentions made by the Company.

I. ESTOPPEL TO URGE INTERSTATE COMMERCE

The Court of Civil Appeals held that under the facts of this case no interstate commerce was involved in the Company's Texas operations; hence the Court did not take notice of the plain estoppel of the Company to raise that issue, reflected by the entire record. Had the Court of Civil Appeals determined that interstate commerce did exist, and had dismissed the interstate commerce defense upon the ground of estoppel, that would not have precluded the Company from urging in this Court both the defense of interstate commerce and the claim of error in the application of the doctrine of estoppel. By similar reasoning the Company is not now precluded from urging the interstate commerce defense in this Court, (unless under our plea of estoppel) nor are appellees precluded from urging the estoppel on that issue. By its silence and acquiescence before the Commission upon the interstate commerce issue the Company led the Commission to believe that the Company was willing to stand or fall only upon the ultimate issues of confiscation, unjustness, and unreasonableness. In presenting before the reviewing courts what amounts in its essence to a gross fraud upon the Commission, and by thus changing the fundamental grounds and theories of its contentions from what they were before the Commission, the Company's attitude upon this entire subject has become plainly untenable.

II. LINE A OPERATIONS AND OKLAHOMA IMPORTATIONS INTO TEXAS DO NOT CONSTITUTE INTERSTATE COMMERCE

The Company fails to distinguish between "transportation," which is a mere incident of commerce, either intrastate or interstate, and "commerce" or "interstate commerce." The gas is not actually sold, or offered for sale, to anyone until it reaches the ultimate consumers at the burner tips—when it is remembered, as it should be, that the Company in the operation of the pipe line business in Texas, and the affiliated distribution companies in the local distribution operations in Texas, are only the agents, automatons, or *alter egos* of the Lone Star Gas Corporation, which is actually carrying on local commerce in Texas, though it has no permit to do so. All operations, from the bottoms of the wells to the burner tips, are carried on by the same integrated set-up, which in reality is the Lone Star Gas Corporation. The railroad and telegraph common carrier cases cited by appellant involved carriage of goods and passengers, or transmission of intelligence, interstate, for other persons for hire; and are, therefore, not in point.

The Company's business, as actually transacted, is wholly intrastate commerce in Texas and Oklahoma respectively. Texas therefore has jurisdiction to regulate such operations in Texas and Oklahoma likewise has co-ordinate jurisdiction to regulate the Company's local business in Oklahoma; because the actual business transacted by the Company in each state respectively is purely local in nature.

The Company, in its latest brief, has attempted to move the Panhandle gas field from Texas into Oklahoma to support its points as to interstate commerce. We prefer to leave the field in Texas, where it actually is.

Line A has been in operation since 1926—approximately twelve years. The two remaining Oklahoma lines (Lines G and 2nd H) through which small quantities of Oklahoma gas are still imported into Texas, have been in operation since 1918 and 1919, respectively, approximately nineteen or twenty years. Rate litigation, involving the Company's operations, has arisen in both states. *Lone Star Gas Company et al v. Corporation Commission of Oklahoma,* 170 Okla. 292, 39 Pac. (2d) 547, 7 P. U. R. N. S. 490. And yet during that period and in the course of such litigation in both states no such conflicts of interest, authority, or jurisdiction have arisen as between the two states as appellant presents to the imagination of this Court. On the contrary, in the present instance, the Texas Commission has entered an order which was materially and unnecessarily generous, both to the Company and to the Oklahoma consumers on the Company's system, in fixing the Texas rate upon an overall basis and thus allowing the Texas rate to be raised substantially above what it should and would otherwise have been, by the allowance for the much more expensive and less profitable Oklahoma operations in setting the Texas rate. The Commission is here proceeding by steps, working toward the fixation of ultimate local burner tip rates in Texas only.

III. CONFISCATION ISSUE—SEGREGATION

The Court of Civil Appeals did not, as the Company represents, hold that any segregation was necessary as between interstate and intrastate commerce; and there is no inconsistency in that Court's opinion in holding on the one hand that no interstate commerce in Texas was involved, and on the other hand that the Company was under the burden of making a segregation between Texas and Oklahoma properties and operations. It is true the Court in several instances referred to the necessity of a segregation between Oklahoma and Texas properties and operations "or interstate and intrastate commerce"—thus perhaps incorrectly using the two terms interchangeably; but a careful analysis of the opinion makes it plain that the Court actually held that such a segregation was necessary only between Oklahoma and Texas properties and operations, and not between interstate and intrastate commerce; as there was no interstate commerce involved, and the Court expressly so held.

The submission of a voluntary segregation by appellees in the District Court, which segregation the Court of Civil Appeals approved, did not, even if such segregation had been held unsound, lift from appellant the burden of making a proper segregation between Oklahoma and Texas properties and operations. *Norfolk & Western Ry. Co. vs. North Carolina*, 297 U. S. 682, 688-689, 80 L. Ed. 977. However, the segregation made by appellees does show that the rate upon the basis of a proper segregation between Texas and Oklahoma is non-confiscatory. Appellant's evi-

dence relating to "overall integrated properties and expenses", if material at all, would have been so only if its *quantum* and *quality* had been of a sufficiently clear, convincing and satisfactory nature—which it was not.

The 85% allocation factor determined by the Court of Civil Appeals was a correct one as between Texas and Oklahoma if a segregation were required to be made. Appellant, however, applies a correct allocation factor to incorrect and unsound bases, to-wit, its own unreasonable valuations and estimates of depreciation, depletion, amortization, operating expenses, revenues, etc. This naturally results in an incorrect segregation. Likewise, the 85% allocation factor was the one worked out by the Commission's witness Freese only upon the overall *properties* in both states *as a whole*. It was not intended to be, and is not, workable when applied only to particular component elements of the property, such as transmission line equipment, or to operating expenses, or depreciation, or revenues, as the Company has attempted to apply it, or imagine the jury as having applied it.

The Company chooses, and insists erroneously that this Court should choose, just any sort of a blended combination of elements of the rate structure as contained in the evidence of both parties, that may be necessary to uphold the jury's verdict; choosing, of course, its own estimates insofar as possible where it thinks its own evidence is by a long stretch of the imagination tenable at all, and choosing on the other hand the elements taken from the appellees' evidence or the Commission's findings where these are more advantageous to the Company, or in lieu of the ele-

ments on which the Company plainly admits by implication that its own evidence was totally inadequate and untenable. This is a novel theory of reviewing the sufficiency of a rate before the courts, and one which so far as we know has never been adopted before, even by contentious litigants, and much less by courts of justice. Thus the Company speculates upon what *may have been* in the minds of twelve lay jurymen, though nothing of the sort is apparent from the jury's actual findings; and even if such things had been in the minds of the jury, they were clearly unsound and incorrect.

The Company argues in effect that whatever the jury's verdict may be in a rate case, regardless of the soundness or unsoundness of the bases and methods of submission to the jury, and regardless of whether the issue of confiscation was requested or actually submitted to and passed upon by the jury or not, the jury's verdict immediately attains final conclusiveness on all parties upon the issue of confiscation, and is not subject to review by the courts through the usual legal analysis of the existence or sufficiency of the evidence to support same. If this contention were sustained, the jury's verdict would end all rate controversies and the courts would have no function to perform or power to exercise in a review and analysis of the evidence. Confiscation would then become only a fact issue for the trial courts, and not at all a law question or a mixed question of law and fact for all the courts. This would result in doing the very thing which the Court of Civil Appeals and this Court and all other courts have held cannot and should not be done, namely, the substitution of the judgment of a trial court not only

for the judgment of the expert legislative body which fixed the rate, but even for the judgment of the reviewing courts—who would, under appellant's theory, be precluded from determining the existence or sufficiency of the evidence to support the verdict or judgment of the trial court. This would, in the final analysis, make the courts, and not the legislative body, the ultimate legislative rate-makers. The Company certainly would not be making any such contentions had the jury's verdict been adverse to it.

The only remaining questions presented to this Court are:

> "1. Did the Company fail to make out its case by not presenting clear and satisfactory evidence?
>
> "2. Does the rate, when properly tested, result in actual confiscation?"

There existed no necessity for a segregation before the Commission, because the Company made before the Commission no claim of interstate commerce, and no objection to the Commission's over-generosity in inquiring into and fixing the rate upon the basis of overall evidence as to Texas-Oklahoma operations, and the Company has thereby misled the Commission upon that point, and in reality perpetrated a fraud both upon the Commission and the courts by its methods adopted herein.

But actually, when proper segregation is made, there is no confiscation shown. Table IV, Appellees' Original Brief, page 199.

At page 20 of its latest brief the Company claims that if Line A operations are left out of account, the return on the remaining Texas intrastate business is shown to be confiscatory. This is not true. Table V, page 200 of Appellees' Original Brief, shows that even the return on West Texas gas (unquestioned intrastate operations) for 1933, which is based on the Company's erroneous segregation between what it chooses to designate as "interstate operations and intrastate operations," was 6.63%. This becomes 6.28% when depreciation correction is made for overall properties as urged at p. 61 of Appellant's First Reply Brief.

The Company frequently but unsuccessfully attempts to fall back upon appellees' evidence to support its contentions. For instance, it falls back upon appellees' evidence to supply the fatal deficiency of its own entire failure to present any evidence for years prior to the depression period 1931-1934; and also in its highly imaginative and speculative combinations or "blendings" of the evidence in such way that it contends the jury "could have found" the evidence clear and satisfactory as to "unreasonableness and unjustness"—and even as to "confiscation," which was not submitted or found at all.

For cancelled and surrendered leases the Commission allowed an average or amortized figure of $99,140.73 in operating expenses, arrived at by the average for the five-year period ending December 31, 1931. In connection with its table of computations at page 64 of its First Reply Brief, the Company states that it has allowed cancelled and surrendered lease expenses, in such

table, as the Commission amortized them; and this statement is repeated on pages 23-24 of Appellant's Second Reply Brief. The statements read fine if taken at face value, but they are not true. Reference to Record III, 2285, shows that the figures there shown as "Available for Depreciation, Depletion, Federal Income Tax and Return" are identical with the figures as they appear under the same heading on page 64 of Appellant's First Reply Brief. The Company has included in that tabulation the correct amount of $99,-140.73 for the year 1931, *but for all subsequent periods it has used amounts substantially in excess of that amount*. How these increased amounts are arrived at, we are unable to discover; but they certainly do not conform to the Commission's findings as the Company proposes. It is deplorable that the Company cannot, or will not, stay with the facts, and that thereby it puts us to the necessity of pointing out its errors a second and third time in order to prevent this Court from being seriously misled.

With respect to claims for Federal Income Tax, the Company again departs materially from the Commission's findings and from any basis fairly supported by the evidence. If the Company had applied the Commission's findings, as it purports to do, it would have deducted no federal income tax, for the Commission expressly finds none would be due under the 32c rate after all allowable deductions are taken. The Company, further, would have the Court believe that the testimony of its own witness, Hulcy, to the effect that approximately $52,000.00 would have been the correct amount of computed federal income tax for the

year 1931, was not true, and is not to be accepted or given any effect by the Court, because such testimony was given by Hulcy on cross examination rather than direct examination. Our previous statements are sufficient to show that the Company has never actually paid to the Government, nor has the Lone Star Gas Corporation ever paid to the Government for Lone Star Gas Company, any such amounts of Federal Income Tax as the Company computes and uses in its tabulations. What this record does reflect, is that the Company has made no payments of income tax direct to the Government at all; but only that the Lone Star Gas Corporation has rendered to the Government consolidated tax returns for the years here under review, for all of its underlying affiliated companies; that no payments have actually been made to the Government upon such returns for any year here under review, with the exception of one or two; that the total amounts actually paid, or actually and justly due, by the *Corporation* for the years in question upon such consolidated returns are not shown by this record at all; that the amount of such actual tax is still in dispute as between the Government and the Corporation for most of the years in question; and that nothing is shown in this record with respect to the methods or soundness of the allocations upon which the Corporation purported to charge to the Company allocated parts of the tax as computed or paid; the Company only making "dummy" or memorandum returns, not to the Government but to the Corporation, upon the erroneously assumed basis that the Company was making a separate return of its own to the Government; and the erroneous, excessive and fictitious

amounts thus computed and allocated to the Company by the Corporation are what the Company has charged into its tabulations here submitted as well as its previous tabulations.

We ask the Court again to remember that,

1. The 32c rate has never been put into actual operation so that we may know what it would have yielded during any period;

2. The theoretical application by the evidence here, of the 32c rate to the Company's actual operations, covers only a period of six or seven months subsequent to the effective date of the order—namely, from September 13, 1933, to April 30, 1934;

3. All of such theoretical applications of the 32c rate subsequent to December 31, 1930, cover only subnormal depression years, and include 1933, the worst financial year of the Company's history, doubly subnormal because of economic depression and abnormally high temperatures.

When all the things are kept in mind, which we have urged in our three briefs here, there can be no doubt whatever that the Company has, as the Court of Civil Appeals held, failed as a matter of law to submit the requisite quantum or quality of clear and convincing evidence to prove confiscation; and, further,

that the rate when properly tested does not result in confiscation.

Respectfully submitted,

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